RICHARD RUSSELL'S DOW THEORY LETTERS INCORPORATED

Since 1958 •

Post Office Box 1759, La Jolla, California 92038

26 Letters Per Year • $250 annually

Nov. 18, 1998 **LETTER 1265**

Nov. 6 DJIA 8975.46; PTI 5314; A-D Ratio +6.09
Nov. 13 DJIA 8919.59; PTI 5309; A-D Ratio +5.42
Dow Yield: 1.69%; Dow Price/Earnings: 24.0
Dow 144-day MA: 8623; Dow 34-day MA: 8380
Dow Times Book Value: 5.59; PTI 89-day MA: 5294
Percentage of Undervalued Blue-chips: 4%
Gold 34-day MA: 297

THE PICTURE: I watch a slew of indices and indicators, but the following SIX are the ones that I consider the most important. The D-J Industrials, D-J Transports, D-J Utilities, Treasury Bonds, advance-decline ratio (for the NYSE), and my Primary Trend Index (yes, I watch the Nasdaq, the Amex, money supply, short interest, margin accounts, you name it, but the SIX listed above are the indicators which I most depend on -- and note that they are all based on market action). So saying, let's take a look at each of them.

First, we see the Dow. From its bull market peak of 9337.97 (July 17) the Dow plunged to an August 31 low of 7539.07. From there the Dow recovered in a violent rally to 8975.46 (Nov. 6). Thus, the Dow recovered an impressive 80% of its bear market losses, but the Dow has not, so far, advanced to, or above, its April bull market high.

The D-J Transports -- they topped out at 3686.02 back on April 16. By October 8 the Transports had fallen to a low of 2345.00. Since then the Transports have rallied to 2968.48, representing a recovery of not quite half (47%) of their previous losses.

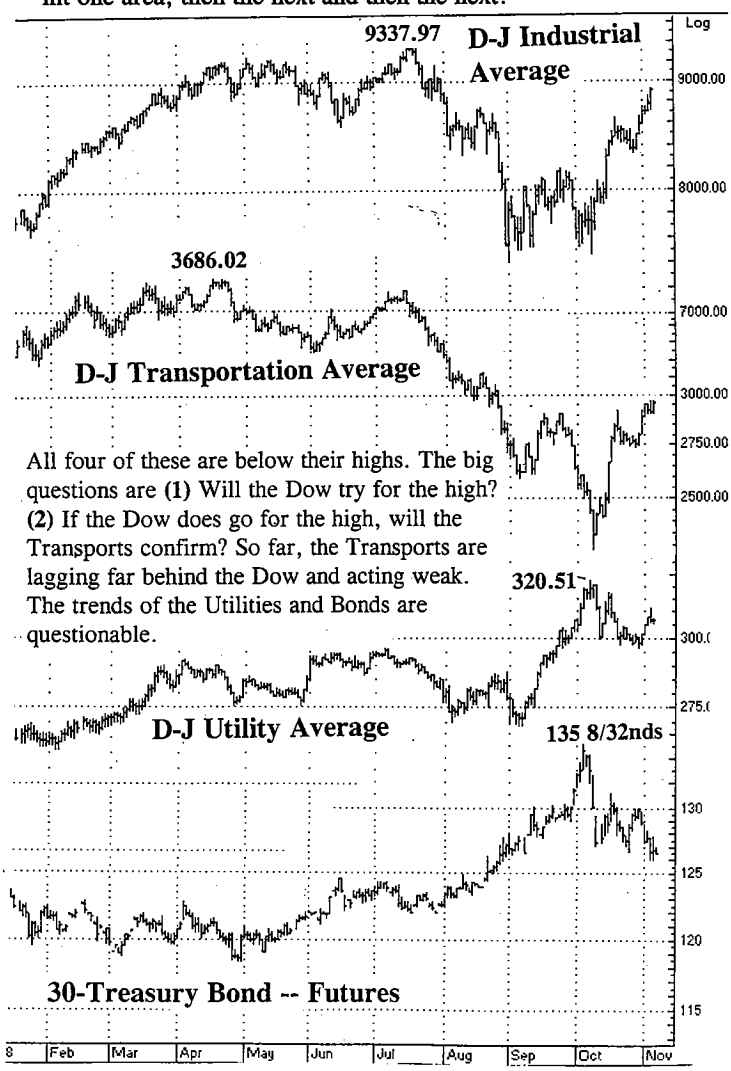
The Transports have consistently been the **KEY** to this bear market. Remember, the Transports refused to confirm the new Dow high in mid-July, setting up a dangerous situation. After that non-confirmation, the Averages turned down and on August 4 the Dow Theory signaled a bear market. In October the Transports broke to a new bear market low, but the Dow refused to confirm. That triggered the latest rally. Now the Dow has advanced to within shooting distance of its bull market high, but the Transports, having failed to recoup even half of their bear market losses, are **again appearing weak.** If, for the sake of argument, the Dow does advance to a new high (above 9337.97) the Transports almost surely would not confirm -- this would set up another dangerous upside non-confirmation. The key -- **watch the Transports** (something very few analysts do).

I have stated that a primary bear market is now in force. I also stated that we have no way of knowing what form the bear market will take or how much time will be required before the bear market fully expresses itself. **Question:** What would it take to prove me wrong in my bear market thesis? The **answer** is simple -- if the advance continues, and **both** the Dow and the Transports rise to new highs, then it would be clear that we have been experiencing a nasty secondary correction within a continuing bull market, rather than the first leg of a bear market. I don't think that's the way it's going to work out, but I'm bound by reality, not by ego. In other words, if I'm wrong, I want the market to prove that I'm wrong. So far it has not.

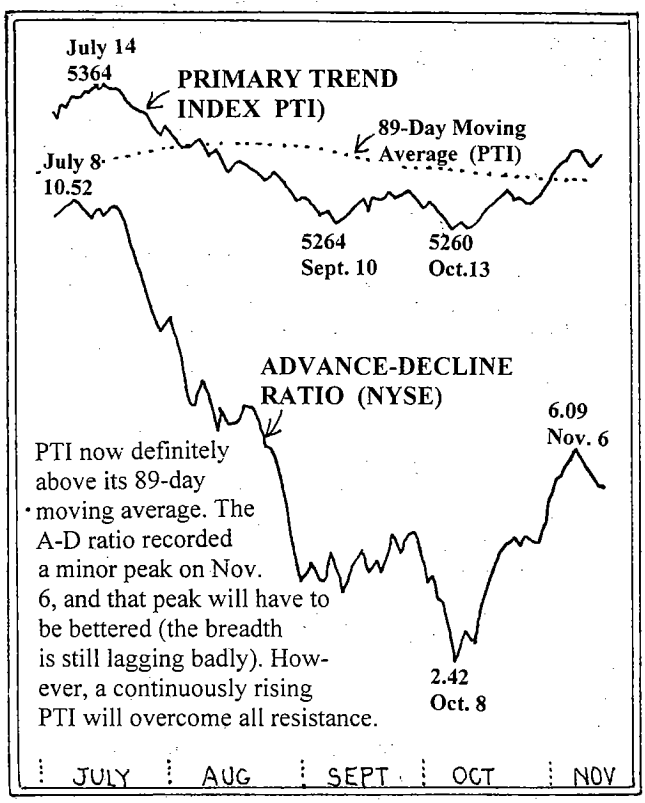
Next we have the D-J Utility Average. In the past, this Average has often been a bellwether, not always, but often. The Utility Average hit its bull market high of 320.51 on October 8. Since then it has backed off, then fluctuated within a narrow range. It will be an obvious plus if the Utility Average can advance to a new high. It will be a minus if the Utility Average closes below 297.86. Ah, all those "ifs."

The fourth chart shows the "long" (30-year) Treasury bond. Every investment is competitive with every other investment, but two of the fiercest competitors are stocks and bonds. And the basic competition has to do with yields. *A few weeks ago almost every analyst was predicting lower interest rates.* Ironically, the bonds now look a bit toppy, and the yield on the long T-bond has moved up -- it's now at 5.28% (this is a guaranteed yield free of state taxes). That 5.28% compares with the minuscule non-guaranteed, taxable yield of 1.48% for the S&P 500.

Dividing bond yields by stock yields gives us a ratio of 3.57 -- in favor of bonds. In other words, for every dollar in dividends you receive from stocks, you receive 3.57 dollars in interest from bonds. Historically, that's been a dangerous ratio for the stock market (but to be honest, this stock market has already ignored a carload of dangerous statistics). Incidentally, the recent "unexpected" swoon in bonds has cost bond traders a lot of money, but isn't that the way bear markets work -- first they hit one area, then the next and then the next?



All four of these are below their highs. The big questions are (1) Will the Dow try for the high? (2) If the Dow does go for the high, will the Transports confirm? So far, the Transports are lagging far behind the Dow and acting weak. The trends of the Utilities and Bonds are questionable.



Now we come (see page 2 chart) to my **Primary Trend Index.** On October 30 the PTI pushed above its 89-day moving average. This was an important signal, a signal that the trend of the market had turned bullish, at least in a secondary sense. Remember, the PTI is based strictly on market action, it doesn't care about yields, values, historical ratios or anything else -- except price action. Does the rising PTI say "bull market"? No, the PTI is non-committal, it simply says that the trend is up.

Note: Interestingly and probably significantly, daily new highs on the NYSE have been meager. October 4 saw 82 new highs, the most that we have seen on the entire recovery. Not very impressive in view of the 80% recovery in the Dow.

Finally, we'll examine the all-important advance-decline ratio (page 2 chart). The A-D ratio traces the advancing or declining action of **all the stocks on the NYSE,** and my guess is that the A-D ratio, more than any other index, reflects the performance of the average investor's portfolio.

The A-D ratio hit a bull market high value of 13.00 on April 3. It then turned down in a crushing decline. On October 8 the ratio struck a low of 2.42 for a total loss during the six months of 10.58 points. From its October 8 low, the A-D advanced, recording a value of 6.09 by November 6. Thus, as of November 6, the A-D ratio had recouped only **35%** of its April to October losses. Not a very impressive recovery, at least so far.

The sub-standard recovery in the A-D ratio accounts for the small number of daily new highs that we've seen during the big rally. Remember, late last year while the market was climbing we saw over 600 new highs. Now with the Dow not far from its earlier high, daily new highs hold well below 100.

Conclusion: Under Dow Theory, this is a bear market, and we'll take it to remain a bear market -- unless or until it's **proved** otherwise. The two Averages, Industrials and Transports, struck their last **joint highs** on April 16. At no time since April 16 have BOTH Averages been higher. Seven months have now elapsed since the joint new highs of April 16, and the bear market is still intact. If I'm correct, if **values deteriorate through time in a primary bear market,** then we are drawing closer and closer to a second round of trouble, both in stocks and the economy.

Bottoms: The following listing (courtesy of *Barron's*) is very informative. It provides **bottoming statistics** for all declines in the S&P Industrials of 15% or more going all the way back to 1932 (using month-end closing statistics). Note that at 17 previous bottoms the price/earnings ratio for the S&P Industrials was never higher than 16.3 and half were below 10. Add the inflation rate to the P/E ratios and all bottoms but two were well below 20.

Birth of a Bull

Valuations at market bottoms
(Following a 15% or greater decline in the S&P Industrials)

Date of Bottom*	Decline From Top*	P/E	P/E + Inflation Rate	P/E + Long Bond Yield
October '90	15.5%	12.9	19.16	21.86
November '87	31.8	14.4	18.91	23.69
July '82	25.5	7.7	14.19	21.23
February '78	19.9	8.3	14.64	16.49
December '74	42.0	7.9	20.10	15.49
June '70	32.3	13.6	19.61	20.68
September '66	17.7	14.0	17.49	18.78
June '62	24.3	15.6	16.82	19.63
February '58	16.2	12.4	15.73	15.68
May '49	16.0	5.7	5.30	7.94
April '42	24.8	7.9	20.58	10.37
May '40	29.5	9.7	11.17	12.20
June '39	19.3	15.3	13.38	17.50
March '38	52.1	9.3	8.44	12.05
March '35	19.6	16.3	19.15	19.06
February '33	33.4	14.0	4.05	17.22
June '32	85.7	9.1	-0.41	12.61
Oct. 21, 1998	8.1	25.5	30.54	26.90

*Using month-end closing prices

Now compare these 17 bottoms with the October 21 low of 1998. Here we see that the P/E was a high 25.5 and the P/E plus the inflation rate was 30.54. Historically, bear market bottoms have been characterized by stocks selling at great values, black pessimism on the part of investors and an absence of the public. At the October '98 low the values just weren't there. In fact, ironically, the October '98 figures look more like the statistics you would expect at a top, rather than a bottom.

Russell Conclusion: Currently, we remain in an area characterized by a buying mania and a public that is convinced that the road to financial comfort, safety and independence is through ownership of common stocks. And all the while the stock/bond yield spread remains very wide in favor of bonds.

Schizophrenia: Figure this one -- the bond market is still opting for **extreme safety.** For instance, the yield differential between 10-year Treasuries and the *WSJ's* "high yield bonds" (i.e. junk bonds) is a whopping 5.62% in favor of Treasuries. On the other hand, investors are paying a **sky-high** P/E ratio of 29 for the S&P. Which group is crazy -- bond-buyers or stock- buyers?

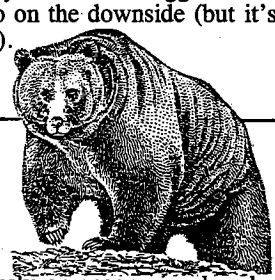
THE BEAR: One study that has gained a large following among analysts over the past few years is the price-to-sales ratio. *Ned Davis Research* put out a special report on September 23 in which they observe that since September, 1990, revenues for the S&P are up just 34% or 3.8% per year. This has taken the price/sales ratio for the S&P from 0.66 to 1.72 -- but the norm for the past four decades has been 0.8. Ned asks, " How in the world can sales grow at such a terribly low rate of 3.8% per annum in what people consider 'the best of all worlds',

especially with new markets opened to the Communist world and with world trade exploding?"

Ned continues, "How can the stock market soar 17.4% per annum while sales of multinational industrial corporations grow only 3.8% per annum?" His conclusion if that the "S&P Industrial price-to-sales ratio shows a record level of optimism by investors." Finally, Ned warns, "Should the 'Goldilocks' economy not hold up, a terrible hangover is possible."

Russell Comment: The record 1.72 price/sales ratio has arrived while sales were still expanding, not expanding nearly fast enough to justify the record 1.72 ratio but nevertheless still expanding.

Now this -- in their September 16 mailing, *ISI* (Ed Hyman and Nancy Lazar) come out with this bombshell: Over the past year, S&P sales have actually **declined** 1% on a year-over-year basis. But what about the record price to sales ratio? Can it possibly hold with sales declining on a year-to-year basis? The sales have dropped below the zero line for the first time since '93. **Russell Comment:** To me, this suggests that the US could be in recession by the first quarter of next year. It also suggests that this bear market has a long way to go on the downside (but it's going to take time, maybe lots of time).



INVESTMENT POSITION: The bear is in the box. After the costly April to October market collapse, he's taking a rest.

When you buy a stock, then consciously or unconsciously what you want is a positive total return on your investment. There are three factors that produce a **total return. (1)** Price/earnings ratios. The P/E ratios are the big swingers in the price of a stock: there's nothing like rising P/E ratios to boost total return. But current problem: the P/E ratio for the S&P is now 29, approximately at the highest level in history. **(2)** Growth in earnings. Rising earnings are great for total return, but problem -- earnings are now in a declining trend. **(3)** Dividends. Personally, I love fat, well-covered dividends. But as I've stated in so many previous Letters, dividend yields today are almost non-existent. Average dividend yields of 1.48% (where they are now) contribute almost nothing to total return. Furthermore, if you buy stocks with average yields of 1.48%, those stocks **had better go up,** otherwise, you are tying up your money in assets which are no better than a summer home which you neither use nor rent. Low-yield stocks that don't go up are simply dead wood. On the other hand, rich dividends allow you to compound. Oh yes, in a bear market there is nothing like a fat, well-covered dividend to put the brakes on your stock when the market turns down.

Currency trading is very tough, and experience tells me that speculating in currencies is doubly difficult for the average investor. Therefore, I generally suggest that my subscribers stay with the old Yankee dollar. The safest place to be in a bear market is in Treasury bills. The bills, admittedly, put you in a very defensive, unexciting position. But in a bear market, you don't need excitement, you need safety.

In a bear market you'll hear a lot about this guy and that person making money during the periodic bear rallies. But you'll hear very little about this guy and that person losing his shirt on the declines. But don't sweat it, that's just human nature. In the end, the bear will have his way -- it's called relieving investors of their assets.

THOSE TRANSPORTS: Transports are diverging again, and I thought it was time for me to write my annual defense of the Transports (I seem to be the last American who believes in the value of the Transports in trend analysis). Ever since I started in this business I've received complaints about the Transportation Average and its value as a confirmatory indicator. "It's antiquated," "It doesn't represent an important segment of the economy," "Who cares about trucking and rails," "What's the trend of transports got to do with the economy?" And on and on.

First, the Transports as a confirming stock average works. **It works!** Time and time again when the Transports confirm or fail to confirm the action of the Industrials, the subsequent action is meaningful. A few Dow Theorists simply claim that it doesn't matter "why," the confirmation principle works, "It just works."

But, of course, there is a rationale behind the confirmation principle. The Industrials represent the productive capabilities of the nation. The Transports represent the sales and transportation capabilities. If you produce but your products don't move or if they are not sold, that equals trouble. By the same token, if you sell but your factories aren't producing what you sell, that equals trouble.

I've said that the D-J Transportation Average has been a bellwether over the last seven months. The Transports failed to confirm the new July bull market high in the Dow and the Transports broke to new lows in September although the Dow did not confirm.

What were the sinking Transports telling us? A recent article in *USA Today* answers the question. They quote a Dallas travel agent, "Deals aren't happening, banks are not lending and lawyers aren't flying . . . An air travel slowdown is just starting, but it is starting." The National Business Travel Association states that companies plan to reduce domestic and international trips, and the average cutback is 20%. Almost 78% of corporations interviewed say they have changed their travel plans in the last 30 days because of bad economic news. Fifty-three percent say they have stepped up video and teleconferencing and 36% have begun to renegotiate contracts with airlines, hotels and car-rental companies." US domestic airline boardings were flat last month compared with September 1997. **Russell Comment:** The Transportation Average does reflect trends in sales and travelling. And those trends are important in confirming trends in manufacturing.

Note: Interestingly, the weak action of the Transports has come while the price of oil has slumped from over 16 bucks a barrel in September down to the current 13.50. Normally, the Transports, particularly the airlines, will surge when the price of oil declines. It's not happening this time, indicating that the Transports are going down for very fundamental reasons, namely, declining traffic.

NOTES & QUOTES: Britain's *Economist* on Clinton and the election: "Yes, he has done it again. You can try to put the man down, load him with inquiries, show him to be a liar and a philanderer, push him into public apologies -- and still he comes back laughing. For the first time since 1822, the party of a Democratic president in his sixth year in office has picked up seats in the House of Representatives . . . Could anyone have predicted it? One man, at least: the Incredible Rebounding President, whose career will leave in the history books a trail inscribed in rubber."

* *

And speaking of prediction, how could the analysts have been so wrong about corporate earnings? Back in January the consensus opinion was that corporate earnings would grow by 15% in 1998. By June they were still of that opinion. Then on August 4, under Dow Theory, the Averages signaled a bear market. Now the third quarter shows earnings down 7%. But analysts, still stubbornly bullish, are predicting earnings up 8% for the fourth quarter and into 1999.

Not so, Salomon Smith Barney. This is from their Nov. 6 "Portfolio Strategist" report: "Over the last few months, we

have seen the downward trend in earnings revision accelerate rapidly. During the last 36 weeks, about 66% of all earnings estimates were revised downward (34% upward) according to I/B/E/S. There had been some speculation, by ourselves and others, that perhaps these downward revisions would prove to be overly pessimistic, thus providing the potential for positive surprises during the third quarter period. Despite the common notion expressed by some that this is indeed what is happening, our work indicates otherwise. Of the 428 companies in the S&P 500 Composite that have reported, less than 36% have recorded an upside surprise. These results are actually worse than the second quarter, when almost 43% of the companies beat their consensus estimates."

* *

All signs suggest a slowing of the economy, this in the face of a rising stock market. The following is from the very prescient *Liscio Report* [(973)509-2256]. "There are already some signs that job growth is slowing -- perhaps slowing significantly. Americans spent more money buying goods and services than they received in after-tax in September, resulting in a negative national personal savings rate for the first time since 1959, when the monthly figures were first published . . . a negative savings rate, coupled with falling consumer confidence and the $1.5 trillion destruction in wealth triggered by the turmoil in the global financial markets, suggest the consumer . . . may turn off the spigot real soon."

* *

What's the nation's (maybe the world's) "hottest" city? On two recent polls, it's **Austin, Texas.** *Newsweek* magazine rated Austin tops in the country for technology. *Fortune* magazine rated Austin the "best city for business," using such criteria as venture capital dollars, job growth, consumer spending and percentage of population with a college degree. San Diego screamed that they should have been in the top 10 (it wasn't), but then Austin has one item that San Diego is sorely missing -- no state income tax. Here in San Diego we have the nation's best weather and close to the nation's worst taxes.

* *

Trade Deficit: According to one of the nation's top trade official, David Aaron, Undersecretary of Commerce for international trade, imports such as textiles from Thailand or footwear from China will continue to grow while US exports, such as construction equipment, will shrink. The main reason he believes the trade deficit will widen will be a decline in US exports, particularly to South America. But it is notable that nearly 30% of US growth comes from exports. And the declining exports will come at a time when the US economy is already losing steam. The Commerce Department is estimating that this year the deficit in goods and services will be $165 billion, up from $110 billion last year. But by some government estimates, the deficit could explode to $300 billion. The previous record for the trade deficit was $153 billion recorded in 1987.

* *

Maybe the biggest **Clinton lie** of the campaign is that all of this year's budget surplus should be left untouched in order to "save" Social Security. Whereupon Clinton spent a billion of the so-called surplus on his various favorite items. As far as saving Social Security, this is a sick joke and BOTH parties (to my disgust) are going along with it. The fact is that SS has been placed in the federal budget and each year, and systematically, the SS surplus is spent by the government. If it were not for the government grabbing the SS surplus, there wouldn't be a budget surplus this year, there would be a deficit of $30 billion. So Clinton's cry of hands off the budget surplus in order to "save" Social Security -- give me a break.

* *

I was talking to a buddy of mine, and I remarked, "Gosh, John Glenn is 77 years old. What would make a guy that old want to take his life in his hands by shooting out into space?" My friend replied, "You know what Glenn said -- it isn't how long you live but how you live." I replied, "I guess I'd vote for both -- quality of life and length." Then I added, "They asked Warren Buffett what he wanted written on his grave stone. Buffett replied, 'I'd like the sentence, **'God, he was old,'** etched on my grave stone.'" Yeah, me too.

* *

I almost never recommend **mutual funds** over individual stocks. First, there are so darn many mutual funds (maybe over 8,000), that it's harder to pick a good fund than a few good stocks. Second, every fund has a management and that management wants to make a profit. The way they make a profit is to take a percentage of the fund's assets. The average fund pulls out 1.5% of assets in fees annually.

But consider this: funds must distribute their realized gains to shareholders every year. A lot of funds locked up taxable profits early in '98, and then in the collapse of August-September they lost money. So the result is that these funds will distribute more in gains than they show in profits. That creates a tax hit for holders of these funds. Seems unfair, but that's the way it works. To simplify, this means that a fund can distribute say three dollars in taxable money but be down 15% for the year. And I don't think most fund owners understand this. No, I'll take individual stocks.

* *

Today there are hundreds of collectors of **old computers.** How about this: The old Apple 1 computer board was the original primitive board created by Steve Jobs and Steve Wozniac in their garage, and only 50 were made. The Apple 1 is a rarity and if you can find one it sells for $30,000.

* *

Russell Peeves: Why can't magazines put their table of contents on the second page so I can find them . . . Why can't the *New Yorker* have funny or at least mildly-funny cartoons like the old days, and why can't the *New Yorker* stop its sycophantic apologies for Clinton . . . Why can't airlines ever be on time? If, per chance, a flight is on time they usually cancel it . . . Why don't they stop dreaming up new athletic events and teams? I've almost given up on professional athletics -- it's become simply a collection of millionaires complaining, striking or changing teams . . . Why can't any newspaper provide a complete run-down on the markets on a single page? The *WSJ* comes close, but not close enough . . . Why does my computer (and it's a good one) always freeze somewhere along the way when I'm on the Internet? . . Why doesn't the milk industry stop those boring milk mustache ads, they've been going for months, and by now I think we get the idea? . . . Why don't the leading cold cereal makers stop boosting the price of their products? I pay $3.45 for branded shredded wheat and $2.15 for the same thing at Trader Joe's (generic). No wonder Kellogg is down from 50 to 35 -- people are tired of getting ripped off on branded cold cereal . . . I never would have believed that people would pay prices of $2.50 and up for fancy coffee, but Starbucks is proving me wrong. But how will SBUX do in the next recession? During the late-1940s when times were tough I used to sit for hours with my buddies at a New York Automat and sip nickel coffee.

* *

The populations of some African nations, Botswana, Zimbabwe, Ghana, have an AIDS infection rate of 25%. Zambia, Swaziland and Namibia are not far behind. This will mean a net decline in their populations over coming years. How did this happen? Their government leaders refused to tell the populace about AIDS or to admit there was an AIDS problem.

* *

This from the very informative *Trident Syndicate* (PO Box 19909, Houston, TX, 77224) written by my old classmate, Donald Morris. "China: Reform Dead in the Water. The huge number of vast, truly antiquated, heavy industry factories, largely owned by the military and operating at grim losses, couldn't be sold at any price -- and couldn't be shut down without throwing fresh millions out of work. As it is there are already 200 million unemployed (and 800 million living on farms who can't make ends meet and leave in droves for the cities) -- Russia, with factories turning out torpedoes nobody needs or wants, has the same problem. To keep the factories going, Zhu was forced to order the banks, already sinking under bad debts, to issue 'policy loans' to enterprises, large and small, drowning in red ink. Privatization, in short, is dead in the water

-- and its corpse is blocking the long-overdue and crucially-needed banking reforms. . . Marxist control of a free-market economy cannot continue indefinitely."

* *

I see that Coke is going into the plastic bottled drinking water business. They had to -- it's become a billion dollar business. I also see that the entire US is now hooked on caffeine, be it in coke, coffee, tea or chocolate. Personally, I'm so sensitive to caffeine that if I drink half a cup of decaf coffee or a cup of tea (both have caffeine) I can feel my pulse jump within minutes. My own instinct is to think that caffeine is a powerful drug, and that most people simply develop a tolerance to it. But that doesn't mean that caffeine isn't dangerous -- I suspect it is (I know it's a powerful diuretic), and a lot of health practitioners tell you to leave it alone.

* *

I've been keeping an eye, actually, both my eyes on the dollar. I think the dollar could be the Achilles heel of the whole economic picture. Consider the following from Peter Bernstein, brilliant editor of *Economic and Portfolio Strategy* [(212)421-8385]. "The international risks revolve round the dollar. The dollar standard has replaced the gold standard in international finance, a role that it has served admirably in recent years . . . The risks to the dollar in lower interest rates are significant. The dollar is the most over-owned asset in the world. The volume of our dollar-denominated liabilities grows every single day. If ever there were an accident waiting to happen, this is it. We are unable to identify what could trigger a dollar crisis, precisely what form such a crisis might take (where would the money go?), or when it might occur, but the consequence would topple many precious applecarts . . . We are not predicting this unhappy outcome, but those bloated international liabilities are there for all to see. The risks to the dollar were present before the Greenspan rate cut, but now the camel has his nose under the tent." **Note**: Consider this, the 11 "euro nations" have a net positive trade balance of $140 billion a year. The US has a negative trade balance for above $100 billion a year. How long can this go on and the dollar still hold up?

* *

A fellow called me from Sioux Falls last week and asked for a trial to Dow Theory Letters. I asked him (as I usually do) how he heard about the Letters. He told me a friend from Boston who gets the Letters told him, "You should read Dow Theory Letters because the guy who writes it is really 'far out'." C'mon, I thought I was conservative. After all, I've sold my motorcycles. And I've always hated debt.

* *

It's getting close, and by January 1 the euro will become the common currency of 11 European nations. But even now, French supermarkets and Belgian banks and Viennese coffee houses are marking their prices in euros, a sure sign that the currency once dismissed as a bureaucratic pipe dream is becoming reality for millions of Europeans. But no one can pay in euros yet, because nobody knows exactly what a euro is worth. They won't know until New Year's Eve; that's the time when finance ministers from the euro-bloc nations will fix the rates. But at this point, it looks like one euro will be worth 6.6 French francs, 1.4 Austrian schillings or 2 German marks. Oh yes, a dollar will be worth about 80 euro cents. It's a bit weird but nobody will be able to buy euros at the banks until 2002; for three years the euro will exist only as a sort of virtual money alongside of the existing currencies. The euro will trade on international markets against the dollar and other currencies. Stock and bond prices will be set in euros. Workers at multinational companies will receive paychecks in euros. Banks will let customers open euro accounts.

* *

By now you must have seen the full-page ads Merrill Lynch is running. In huge black letters they tell us that **"Timing is Nothing."** What arrogance. Merrill's own stock is down from a high of 109 in mid-July to a low of 35 in October; the stock is now around 60. Of course, above all what Merrill wants you to do is keep your investments at Merrill (or in one of Merrill's high commission cost funds) regardless of what the market does. And what if the bear market decimates stocks over the next few years? Will Merrill still blare in headlines that "Timing is Nothing?"

* *

Incidentally, do you wonder why the commentators on FNN, CNN and CNBC tend to have a bullish bias? And have you wondered why there's so little talk of a bear market? The answer, of course, is that the TV gals and guys know that a bear market will mean that the stations will opt for savings and cut-backs. So you can't blame the commentators -- consciously or unconsciously they are well aware that bull markets mean jobs and maybe raises while bear markets mean worries and pink slips.

* *

All eyes are now on **Brazil**. As it prepares to receive the huge IMF bail-out, Brazil has revealed a package of budget cuts and tax increases. But the test is coming: how soon can Brazil cut its interest rates (which start at 40%) while inflation is just 3% without triggering a new run on Brazil's currency, the real? The real is considered to be about 25% overvalued, and is supposed to be devalued in a series of steps. Critics say that no currency pegged to the dollar has been able to withstand major pressure, and Brazil's currency is under pressure. Furthermore, Brazil's current account deficit is running a whopping 4% of GDP.

* *

Unrelated Items: I just received the new portable AM/FM radio manufactured by genius, Henry Kloss. Amazing sound for $199. I recommend it highly -- Cambridge Sound Works [(800)367-4434] . . . I ride daily in my Mercedes 230 SLK, the little convertible with the amazing metal roof -- the car becomes an air-tight coupe in 24 seconds (just press the button). This car is more fun than any car I've ever owned; small but roomy . . . Raves from every quarter for the new S Class Mercedes. This from Britain's *Financial Times*: "If the worst you can say about a car is that you become aware of a small amount of wind noise when its speed tops 125 MPH, it has to be considered well nigh perfect. Which is why the new Mercedes S Class is currently the best saloon car in the world." I'll bet it is, but the price, over 70 grand, will stop a lot of people . . . More and more subscribers with heart trouble are calling me about chelation. The full story of chelation is on the Net. In San Diego, Dr. Michael Leeman offers chelation -- [(619)456-1996] . . . Have you seen the new 20 dollar bill? Have you ever seen a worse design? Who at the Treasury passed on this monstrosity? . . .The *LA Times* will soon join the national edition parade. That means that the *WSJ, USA Today, NY Times* and *LA Times* will all be competing nationally . . . We now have FNN, CNBC and Bloomberg TV running all day long (Bloomberg runs 24 hours). Do you wonder where all those interminable "quarterly earnings meeting expectations" come from? It's kooky, it's crazy, it's actually annoying. It comes from the three TV stations blabbering all day long. When you think about it, what else do these guys have to fill up the long hours? "Hey, Hokey.com missed analysts' expectations by one full cent. Now how 'bout that! Zzzzzz." . . . Two great art exhibits in NYC, Jackson Pollack and Mark Rothko. Wish I was there -- but for one day only . . . All hail Alan Greenspan. He's now considered to be an economic genius. My opinion: in this business it's better to be lucky than smart -- I think Greenspan is smart, but more than that he's been a very, very lucky guy. He's ridden the greatest and longest boom in history. I'm thinking that Greenspan's real test lies ahead . . . The Fed offers a group of seven comic books, and they're very informative (if you're too sophisticated to read 'em, get them for your kids). You think you know it all? How many Fed governors are there? How long are they appointed for? Which Fed bank implements their policy? What are the limits, percentage-wise, that the Fed can order on bank reserves? This is just a tiny sample of what's contained in these informative little comic books. And they're **free.** Write for all seven at the Federal Reserve Bank of NY, Public Information Dept., 33 Liberty St., NY, NY 10045. Like everything else connected with our government, delivery is slow . . . Bill Gates has been a lousy witness for **Microsoft,** but the market doesn't seem to care

at all -- maybe investors think they'd do even better if MSFT was split into three separate divisions.

* *

The man who is effectively running Russia until elections in the year 2000 is Yevgeny Primakov (born Finkelstein). Why does he call himself Primakov? Answer: With anti-Semitism rising in Russia, he'd prefer that Russians didn't know he was a Jew. Primakov, like Yeltsin, has health problems of his own, and observers wonder whether he'll bow out before 2000. Yeltsin has actually bowed out already, and it's announced that the "day-to-day" problems will be addressed by others. In the meantime, Russia has let it be known that it cannot pay its foreign debts and will have to re-negotiate.

* *

With a son at Berkeley, I now have to worry about my youngest daughter, age 18, getting into college. I just received the alumni bulletin from my own alma mater, NYU. I entered NYU right after WWII ended, spent three happy years there and graduated, all courtesy of the GI Bill. In those days, all you needed was a decent high school record and a polite smile and you were accepted. No more. This from the latest NYU alumni bulletin, "A record number of 24,500 undergraduates sought admission to NYU this fall. We accepted fewer than 35%, the lowest admit rate in our history. This is an exciting statistic, because it continues our trend of being more selective in our admissions process. Last year we had an acceptance rate of just under 40%; on all years prior we were over 50%. For this first time, moreover, the average SAT score is above the 1300 mark (1311) for all four-year schools. This represents a significant increase from the 1997 average of 1288." **Russell Comment:** This is typical of what's happening at all top private universities. And then there are the costs, which run up to $30,000 a year including housing. Whew!!

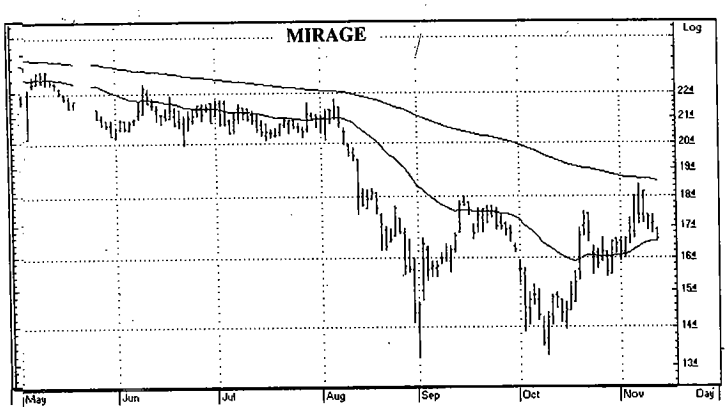
* *

Here's a letter just received (I get a lot of these). "Richard, Just finished Letter #1264. I have been thinking of your advice, and I actually feel sorry for you. You and the BEAR are fighting against the most powerful institutions -- Executive Branch, Legislative Branch -- House and Senate -- both parties, the brightest minds, computers, etc., that money can buy. The IMF, World Bank, Wall Street, Federal Reserve! How can you sleep? Do you realize what you are up against? Good luck, but do you feel the RISK? Who do I believe, Russell, Cohen, Greenspan? A.B.S., Austin, Texas."

Russell reply: You don't have to believe me or Cohen or Greenspan, just believe the market. I've stated what the market would have to do to prove me wrong. As far as "fighting" all those institutions, as I've said so many times, the primary trend of the market is more powerful than the President, the Treasury, the Fed and the Congress all taken together. Remember, nobody wants a bear market, but all the institutions taken together have never been able to stop the bear (or the bull, for that matter -- remember Greenspan's unheeded "irrational exuberance" warning?).

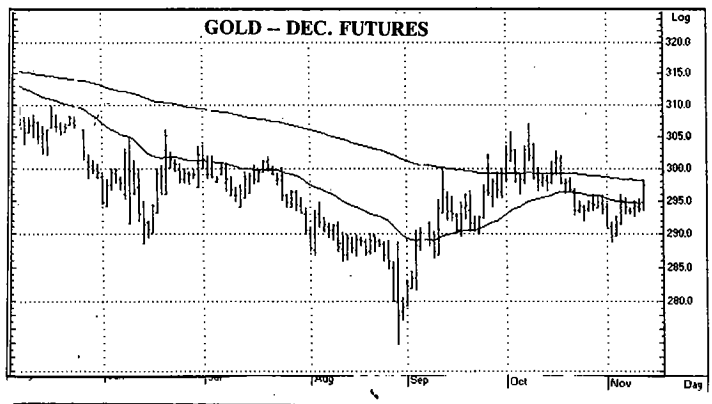
* *

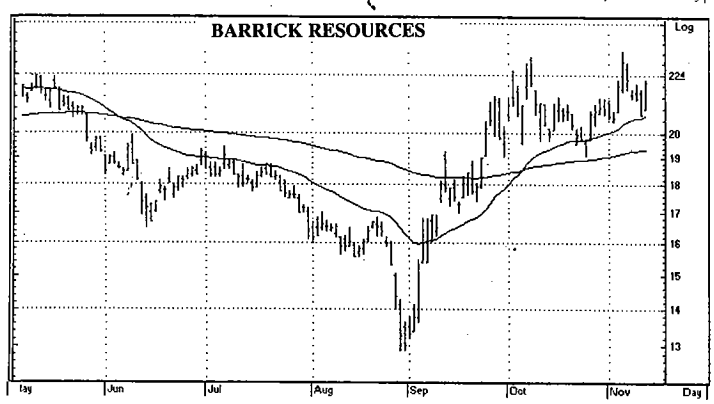
The word I hear out of Las Vegas is that business is slowing down and that Vegas is over-building. I'm fascinated with the new $1.6 billion Bellagio, as the success or failure of this huge investment could tell us a lot about where Vegas is heading. The chart of Mirage (they own Bellagio) should tell us whether Bellagio is going to be a success or not. So far, no new high on MIR to celebrate the opening of Bellagio. Mmmm.



GOLD: As I write, gold is slowly and laboriously pushing higher. How much of this is based on the Iraq situation I don't know, but gold (Dec. futures) has bettered its 34-day moving average and is now pressing against its 144-day MA, which stands at 298. As I see it, if gold betters first 300 and more importantly closes above 305, then we've got a bullish picture. Until then, gold-philes will just have to keep their fingers crossed.

However, the gold shares seem to be telling us something. Barrick Resources looks good and has risen 75% from its late-September low of 13. Placer Dome is the hero of the group, having doubled from its September low. These two would be my choice for anyone wishing to participate in the future of gold. I might add that so far and in recent years the dollar has served as a proxy for gold. If we knew how long faith in the dollar is fated to last, we would know a heck of a lot more about the future of gold.





LATE NOTES: I guess "Slick Willie" thought, "Why make waves, why not give Saddam another chance?" -- his third chance, to be exact. Actually, Saddam is playing Clinton like a violin, and we're dealing with "cheat and retreat" all over again. And why not -- it costs Saddam absolutely nothing while it costs the US billions of dollars for each successive military build-up.

As for the stock market, nothing's bothering the Dow at this point, although something appears to be bothering the Transports (it could be a drop-off in airline or rail traffic). Meanwhile, the absolute frenzy to buy anything even remotely connected to the Internet, regardless of earnings, goes on. The picture reminds me very much of the 1968 maniacal rush into anything tangible (this time it's a rush into anything financial or "inter-netable). Keep your eye on the Transports -- to confirm even in a secondary sense they must better 2968.50.

NEXT MAILING: Dec. 2, 1998